

**DEPARTMENT OF THE TREASURY  
Office of the Comptroller of the Currency  
12 CFR Part 4  
[Docket No. 99-13]  
RIN 1557-AB60**

**FEDERAL RESERVE SYSTEM  
12 CFR Part 211  
[Regulation K; Docket No. R-1012]**

**FEDERAL DEPOSIT INSURANCE CORPORATION  
12 CFR Part 347  
RIN 3064-AC15**

**Extended Examination Cycle For U.S. Branches and Agencies of Foreign Banks**

**AGENCIES:** Office of the Comptroller of the Currency, Treasury; Board of Governors of the Federal Reserve System; and the Federal Deposit Insurance Corporation.

**ACTION:** Joint final rule.

**SUMMARY:** The Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), and the Federal Deposit Insurance Corporation (FDIC) (collectively, the Agencies) are adopting as a joint final rule their joint interim rule implementing section 2214 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA). Section 2214 of EGRPRA authorizes the Agencies to extend the examination cycle for certain United States branches and agencies of foreign banks. This joint final rule makes United States branches and agencies of foreign banks with total assets of \$250 million or less eligible for an 18-month examination cycle if they meet certain qualifying criteria.

**EFFECTIVE DATE:** October 22, 1999.

**FOR FURTHER INFORMATION CONTACT:**

OCC: Martha Clarke, Senior Attorney, International Activities (202/874-0680); Jose Tuya, Director, International Banking & Finance (202/874-4730); or Karl Betz, Attorney, Legislative and Regulatory Activities (202/874-5090), Office of the Comptroller of the Currency, 250 E Street SW., Washington, D.C. 20219.

Board: Barbara J. Bouchard, Manager, Division of Banking Supervision and Regulation (202/452-3072); or Jonathan D. Stoloff, Counsel, Legal Division (202/452-3269), Board of Governors of the Federal Reserve System, 20th Street and

Constitution Avenue NW., Washington, D.C. 20551.

FDIC: Karen Walter, Chief, International Branch, Division of Supervision (202/898-3540); or Mark Mellon, Counsel, Regulation and Legislation Section, Legal Division (202/898-3854), Federal Deposit Insurance Corporation, 550 17th Street NW., Washington, D.C. 20429.

## **SUPPLEMENTARY INFORMATION:**

### **Background**

The International Banking Act of 1978 (the IBA),<sup>1</sup> as amended by the Foreign Bank Supervision Enhancement Act of 1991,<sup>2</sup> prescribed a 12-month examination schedule for U.S. branches and agencies of foreign banks. Section 2214 of EGRPRA modified that requirement by amending section 3105(c)(1)(C) of the IBA to provide that U.S. branches and agencies of foreign banks are subject to on-site examination as frequently as national banks and state banks are examined by their appropriate federal banking agencies.<sup>3</sup>

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<sup>1</sup>Pub. L. 95-369, 92 Stat. 607.

<sup>2</sup>Pub. L. 102-242, 105 Stat. 2286.

<sup>3</sup>Section 2214 of EGRPRA, Pub. L. 104-208, 110 Stat. 3009. Section 3105(c)(1)(C) is codified at 12 U.S.C. 3105(c)(1)(C).

In general, national banks and state banks must be examined every 12 months. However, section 111 of the Federal Deposit Insurance Corporation Improvement Act of 1991<sup>4</sup> authorized an 18-month examination cycle for certain national banks and state banks with a composite rating of 1 under the Uniform Financial Institutions Rating System (UFIRS) and total assets of \$100 million or less. Subsequently, section 306 of the Riegle Community Development and Regulatory Improvement Act of 1994<sup>5</sup> expanded the availability of the 18-month examination cycle to certain national banks and state banks with a composite rating of 1 under UFIRS and total assets of less than \$250 million, as well as to certain national banks and state banks with a composite rating of 2 under UFIRS and total assets of \$100 million or less. Finally, section 2221 of EGRPRA amended section 10(d) of the Federal Deposit Insurance Act (FDI Act)<sup>6</sup> to provide that at any time after September 23, 1996, U.S. bank supervisory agencies could extend the 18-month examination cycle to certain national banks and state banks with a composite rating of 2 and total assets of \$250 million or less. Effective April 2, 1998, the Agencies issued a final rule that extended the examination cycle to 18 months for certain national banks and state banks that satisfy the requirements of section 2221 of EGRPRA. 63 FR 16377 (April 2, 1998). To be eligible for the extended cycle, the national bank or state bank must:

- (a) Have total assets of \$250 million or less;
- (b) Be rated a composite 2 or better under the UFIRS;
- (c) Be well capitalized;
- (d) Be well managed;
- (e) Not be subject to a formal enforcement action; and
- (f) Not have experienced a change of control during the preceding 12-month period in which a full-scope, on-site examination would have been required but for section 10(d) of the FDI Act.

### **Interim Rule**

To implement section 2214 of EGRPRA, the Agencies issued a joint interim rule on August 28, 1998, that similarly extended the examination cycle for certain U.S. branches and agencies of foreign banks. 63 FR 46118. Under the joint interim rule, a U.S. branch or agency of a foreign bank may be considered for an 18-month examination cycle if the branch or agency meets certain criteria and if there are no other factors that cause the appropriate federal banking agency to conclude that more frequent examinations of the branch or agency are appropriate. To be eligible for an 18-month examination cycle, the U.S. branch or agency of a foreign bank must:

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<sup>4</sup>Pub. L. 102-242, 105 Stat. 2236 (section 111 is codified at 12 U.S.C. 1820(d)).

<sup>5</sup>Pub. L. 103-325, 108 Stat. 2160.

<sup>6</sup>Section 10(d) of the FDI Act is codified at 12 U.S.C. 1820(d)(10).

- (a) Have total assets of \$250 million or less;
- (b) Have received a composite ROCA<sup>7</sup> supervisory rating of 1 or 2 at its most recent examination;
- (c) Satisfy the requirements of either paragraph (1) or (2):
  - (1) The foreign bank's most recently reported capital adequacy position consists of, or is equivalent to, Tier 1 and total risk-based capital ratios of at least 6 percent and 10 percent, respectively, on a consolidated basis; or
  - (2) The branch or agency has maintained, on a daily basis over the past three quarters, eligible assets in an amount not less than 108 percent of third party liabilities (determined consistent with applicable federal and state law) and sufficient liquidity is currently available to meet its obligations to third parties;
- (d) Not be subject to a formal enforcement action or order by the Board, FDIC, or OCC; and
- (e) Not have experienced a change in control during the preceding 12-month period in which a full-scope, on-site examination would have been required but for section 3105(c)(1)(C) of the IBA.

The Agencies noted in the joint interim rule that each Agency retains the authority to examine a U.S. branch or agency of a foreign bank as frequently as the Agency deems necessary. The joint interim rule also provided that, in determining whether a U.S. branch or agency of a foreign bank is eligible for an extended examination cycle, the Agencies may consider additional factors, including whether:

- (a) Any of the individual components of the ROCA rating of the U.S. branch or agency is rated 3 or worse;
- (b) The results of any off-site supervision indicate a deterioration in the condition of the U.S. branch or agency;
- (c) The size, relative importance, and role of a particular U.S. branch or agency when reviewed in the context of the foreign bank's entire U.S. operations otherwise necessitate an annual examination (including, for example, whether the office generates a significant level of assets that are booked elsewhere); and
- (d) The condition of the foreign bank itself gives rise to a need to examine the U.S. branch or agency every 12 months.

The Agencies noted further that they generally will determine whether to apply the 18-month examination cycle to a particular U.S. branch or agency based on the overall risk assessment for that office, as well as the factors noted in the joint interim rule.

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<sup>7</sup>The supervisory rating system for branches and agencies of foreign banks is referred to as ROCA. The four components of ROCA are: risk management, operational controls, compliance, and asset quality.

Since U.S. branches and agencies of foreign banks do not receive separate examination ratings of their management, the Agencies stated in the joint interim rule that they will use certain criteria as a proxy for the well managed criterion applicable to U.S. banks, including the ROCA component and composite ratings, the existence of any formal enforcement action or order issued by an Agency, and the other discretionary standards described in the preceding paragraph.

The joint interim rule became effective immediately, but the Agencies invited public comment on any aspect of the joint interim rule. As discussed in the following paragraphs, the commenters strongly favored adopting the expanded examination cycle as set forth in the joint interim rule.

### **Comments Received**

In response to their request for comment on the joint interim rule, the Agencies received a total of seven comments, including six from banks and one from a trade association. The commenters strongly supported the expanded examination cycle for U.S. branches and agencies of foreign banks. They agreed that the expanded examination cycle would reduce regulatory burden on smaller, well-run branches and agencies that do not pose significant supervisory concerns.

One commenter, while expressing support for the rule, requested that the Agencies clarify four points.

First, the commenter sought clarification that the two tests for determining whether a branch or agency is well capitalized are alternative tests and that use of one test for one examination cycle does not preclude use of the other test in subsequent examination cycles. The commenter is correct. The criterion based on capital states that the U.S. branch or agency must satisfy the requirements of either test. Reliance on one of the eligibility tests for an extended examination cycle does not preclude subsequent reliance on the other test. The two capital adequacy tests contained in this rule are limited in their applicability to determining whether a branch or agency is eligible for an extended examination cycle. These two capital adequacy tests have no effect on special asset maintenance requirements.

Second, the commenter also requested guidance as to how the ~~well~~ capitalized criterion will be implemented. Capital adequacy will be determined using regulatory and supervisory reports, and public information where appropriate. The foreign bank's capital adequacy may be assessed on the basis of the home country supervisor's capital standards if those standards are in all respects consistent with the Basel Accord.

Third, the commenter requested that the Agencies clarify whether both eligible assets and average third party liabilities are to be determined consistent with applicable federal and state law. The commenter noted that the wording of the alternative capital test

using eligible assets in the interim rule suggested that average third party liabilities were not to be determined in accordance with applicable federal and state law. The Agencies have amended that provision in the final rule to clarify that both eligible assets and average third party liabilities are to be determined consistent with applicable federal and state law.

Finally, the commenter asked how the Agencies would determine the sufficiency of a branch's or agency's liquidity under the alternative capital test. The alternative capital test measures eligible assets against average third party liabilities over the past three quarters. The requirement that sufficient liquidity is available to meet obligations to third parties is designed to ensure that the branch or agency is able to meet unexpected demands in the event of a sudden economic downturn or other adverse events affecting the foreign bank or its U.S. offices subsequent to the last quarter measured under the alternative capital test. Accordingly, determinations regarding the sufficiency of a branch's or agency's liquidity need to be made on a case-by-case basis.

### **Final Rule**

In light of the comments received, the Agencies are adopting the joint interim rule as a joint final rule with the clarifications discussed above. Under the joint final rule, in order to be eligible for the extended examination cycle, a U.S. branch or agency of a foreign bank must:

- (a) Have total assets of \$250 million or less;
- (b) Have a composite ROCA supervisory rating of 1 or 2 at its most recent examination;
- (c) Meet either of the ~~well~~ capitalized criteria noted above;
- (d) Not be subject to a formal enforcement action or order by the Board, FDIC, or OCC; and
- (e) Not have undergone a change in control during the preceding 12-month period in which a full-scope, on-site examination would have been required but for section 3105(c)(1)(C) of the IBA. For purposes of this rule, a branch or agency of a foreign bank will be deemed to have undergone a change in control if it is sold to another foreign bank or if there has been a change in control of the foreign bank.

The Agencies may consider other factors in determining whether a U.S. branch or agency that meets the foregoing criteria should not be eligible for an extended examination cycle. These discretionary factors include whether:

- (a) Any of the individual components of the ROCA rating of the U.S. office is rated 3 or worse;
- (b) The results of any off-site supervision indicate a deterioration in the condition of the office;
- (c) The size, relative importance, and role of a particular office when reviewed in the context of the foreign bank's entire U.S. operations otherwise necessitates an annual

examination (including, for example, whether the office generates a significant level of assets that are booked elsewhere); and

- (d) The condition of the foreign bank itself gives rise to such a need.

The Agencies will base their determination whether to apply the 18-month examination cycle to a particular U.S. branch or agency on the overall risk assessment for that office. Each Agency retains the authority to examine a branch or agency within its jurisdiction as frequently as the Agency deems necessary. Thus, for instance, the appropriate Agency may determine that changes in the level or direction of risk in a branch or agency or in the level of third party liabilities may warrant examining the branch or agency before the expiration of an 18-month exam cycle.

The Agencies believe that an extended examination cycle for eligible U.S. offices of foreign banks is consistent with principles of safety and soundness because it will permit the Agencies to focus their resources on those offices that present the most immediate supervisory concerns while concomitantly reducing the regulatory burden on smaller offices that do not pose a similar level of concern. The Agencies will continue to use off-site supervision techniques, including the submission of regulatory reports, to monitor the condition and any changes in the risk profile of offices scheduled to be examined on the extended 18-month examination cycle.

### **Immediate Effective Date**

The Agencies find good cause for dispensing with the 30-day delayed effective date prescribed by the Administrative Procedure Act (APA), 5 U.S.C. 551 *et seq.* The expanded examination cycle was effective upon publication of the joint interim rule in August 1998. This joint final rule adopts the interim rule with minor changes. While the Agencies invited interested parties to comment on the rule at that time, each Agency already has implemented the expanded examination cycle. Accordingly, depository institutions will not require any additional time to adjust their policies or practices in order to comply with the joint final rule.

### **Regulatory Flexibility Act**

A regulatory flexibility analysis under the Regulatory Flexibility Act is only required when an agency is required to publish a general notice of proposed rulemaking for any proposed rule. 5 U.S.C. 603. As noted previously, the Agencies have determined that it was not necessary to publish a notice of proposed rulemaking for this joint final rule. Accordingly, a regulatory flexibility analysis is not required.

### **Small Business Regulatory Enforcement Fairness Act**

Title II of the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA)<sup>8</sup> provides generally for agencies to report rules to Congress and the General

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<sup>8</sup>Pub. L. 104-121.

Accounting Office (GAO) for review. The reporting requirement is triggered when a Federal Agency issues a final rule. The Agencies filed the appropriate reports with Congress and the GAO as required by SBREFA. The Office of Management and Budget has determined that the joint final rule does not constitute a ~~A~~major rule@as defined by SBREFA.

#### **Paperwork Reduction Act**

In accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3501 *et seq.*), the Agencies have determined that no collections of information pursuant to the Paperwork Reduction Act are contained in this joint final rule.

#### **OCC Executive Order 12866 Statement**

The OCC has determined that this final rule is not a significant regulatory action under Executive Order 12866.

#### **OCC Unfunded Mandates Act of 1995 Statement**

Section 202 of the Unfunded Mandates Reform Act of 1995, Pub. L. 104-4, 109 Stat. 48 (March 22, 1995) (Unfunded Mandates Act), requires that an agency prepare a budgetary impact statement before promulgating a rule that includes a Federal mandate that may result in the expenditure by state, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year. If a budgetary impact statement is required, section 205 of the Unfunded Mandates Act also requires an agency to identify and consider a reasonable number of regulatory alternatives before promulgating a rule. Because the OCC has determined that this joint final rule will not result in expenditures by state, local, and tribal governments, in the aggregate, or by the private sector, of \$100 million or more in any one year, the OCC has not prepared a budgetary impact statement or specifically addressed the regulatory alternatives considered. As discussed in the preamble, this joint final rule will have the effect of reducing regulatory burden on certain national banks.

### **LIST OF SUBJECTS**

#### **12 CFR Part 4**

Freedom of information, Organization and functions (Government agencies), Reporting and recordkeeping requirements.

#### **12 CFR Part 211**

Exports, Federal Reserve System, Foreign banking, Holding companies, Investments, Reporting and recordkeeping requirements.

#### **12 CFR Part 347**

Allocated transfer risk reserve, Banks, banking, Bank deposit insurance, Bank mergers, Credit, Foreign banking, Foreign branches, Foreign investments, Insured



branches, International lending, International operations, Investments, Reporting and recordkeeping requirements.

## **Office of the Comptroller of the Currency**

### **12 CFR Chapter I**

#### **Authority and Issuance**

For the reasons set forth in the joint preamble, part 4 of chapter I of title 12 of the Code of Federal Regulations is amended as follows:

#### **PART 4--ORGANIZATION AND FUNCTIONS, AVAILABILITY AND RELEASE OF INFORMATION, CONTRACTING OUTREACH PROGRAM**

Accordingly, the interim rule amending 12 CFR Part 4, which was published at 63 FR 46118 on August 28, 1998, is adopted as a final rule with the following changes.

1. The authority citation for part 4 continues to read as follows:

**Authority:** 12 U.S.C. 93a. Subpart A also issued under 5 U.S.C. 552; 12 U.S.C. 481, 1820(d), and 3105(c)(1). Subpart B also issued under 5 U.S.C. 552; E.O. 12600 (3 CFR, 1987 Comp., p. 235). Subpart C also issued under 5 U.S.C. 301, 552; 12 U.S.C. 481, 482, 1821(o), 1821(t); 18 U.S.C. 641, 1905, 1906; 31 U.S.C. 9701. Subpart D also issued under 12 U.S.C. 1833e.

2. In ' 4.7, paragraphs (b)(1)(iii)(B) and (b)(2) introductory text are revised to read as follows:

#### **' 4.7 Frequency of examination of Federal agencies and branches.**

\* \* \* \* \*

(b) \* \* \*

(1) \* \* \*

(iii) \* \* \*

(B) The branch or agency has maintained on a daily basis, over the past three quarters, eligible assets in an amount not less than 108\_percent of the preceding quarters average third party liabilities (determined consistent with applicable federal and state law), and sufficient liquidity is currently available to meet its obligations to third parties;

\* \* \* \* \*

(2) Discretionary standards. In determining whether a Federal branch or agency

that meets the standards of paragraph (b)(1) of this section should not be eligible for an 18-month examination cycle pursuant to this paragraph (b), the OCC may consider additional factors, including whether:

\* \* \* \* \*

September 17, 1999

(signed) John D. Hawke, Jr.

Date: \_\_\_\_\_ John D.  
Hawke, Jr.,

\_\_\_\_\_  
Comptroller of the Currency.

## **Federal Reserve System**

### **12 CFR Chapter II**

#### **Authority and Issuance**

For the reasons set forth in the joint preamble, the Board amends 12 CFR Part 211 as follows:

### **PART 211--INTERNATIONAL BANKING OPERATIONS (REGULATION K)**

#### **Subpart B--Foreign Banking Organizations**

Accordingly, the interim rule amending 12 CFR Part 211, which was published at 63 FR 46118 on August 28, 1998, is adopted as a final rule with the following changes.

1. The authority citation for part 211 continues to read as follows:

**Authority:** 12 U.S.C. 221 et seq., 1818, 1835a, 1841 et seq., 3101 et seq., and 3901 et seq.

2. In ' 211.26, paragraphs (c)(2)(i)(C)(2) and (c)(2)(ii) introductory text are revised to read as follows:

**' 211.26 Examination of offices and affiliates of foreign banks.**

\* \* \* \* \*

(c) \* \* \*

(2) \* \* \*

(i) \* \* \*

(C) \* \* \*

(2) The branch or agency has maintained on a daily basis, over the past three quarters, eligible assets in an amount not less than 108 percent of the preceding quarter's average third party liabilities (determined consistent with applicable federal and state law) and sufficient liquidity is currently available to meet its obligations to third parties;

\* \* \* \* \*

(ii) Discretionary standards. In determining whether a branch or agency of a foreign bank that meets the standards of paragraph (c)(2)(i) of this section should not be eligible for an 18-month examination cycle pursuant to this paragraph (c)(2), the Board

may consider additional factors, including whether:

\* \* \* \* \*

By Order of the Board of Governors of the Federal Reserve System,  
October 12, 1999.

(signed) Jennifer J. Johnson

Jennifer J. Johnson,  
Secretary of the Board.

## **Federal Deposit Insurance Corporation**

### **12 CFR Chapter III**

#### **Authority and Issuance**

For the reasons set forth in the joint preamble, the Board of Directors of the FDIC amends part 347 of chapter III of title 12 of the Code of Federal Regulations as follows:

#### **PART 347--INTERNATIONAL BANKING**

1. The authority citation for part 347 continues to read as follows:

**Authority:** 12 U.S.C. 1813, 1815, 1817, 1819, 1820, 1828, 3103, 3104, 3105, 3108; Title IX, Pub. L. No. 98-181, 97 Stat. 1153.

2. Section 347.214 is revised to read as follows:

#### **' 347.214 Examination of branches of foreign banks.**

(a) Frequency of on-site examination. Each branch or agency of a foreign bank shall be examined on-site at least once during each 12-month period (beginning on the date the most recent examination of the office ended) by:

- (1) The Board of Governors of the Federal Reserve System (Board);
- (2) The FDIC, if an insured branch;

(3) The Office of the Comptroller of the Currency (OCC), if the branch or agency of the foreign bank is licensed by the Comptroller; or

(4) The state supervisor, if the office of the foreign bank is licensed or chartered by the state.

(b) 18-month cycle for certain small institutions. (1) Mandatory standards. The FDIC may conduct a full-scope, on-site examination at least once during each 18-month period, rather than each 12-month period as provided in paragraph (a) of this section, if the insured branch:

(i) Has total assets of \$250 million or less;

(ii) Has received a composite ROCA supervisory rating (which rates risk management, operational controls, compliance, and asset quality) of 1 or 2 at its most recent examination;

(iii) Satisfies the requirement of either the following paragraph (b)(iii)(A) or (B):

(A) The foreign bank's most recently reported capital adequacy position consists of, or is equivalent to, Tier 1 and total risk-based capital ratios of at least 6 percent and 10 percent, respectively, on a consolidated basis; or

(B) The insured branch has maintained on a daily basis, over the past three quarters, eligible assets in an amount not less than 108 percent of the preceding quarter's average third party liabilities (determined consistent with applicable federal and state law) and sufficient liquidity is currently available to meet its obligations to third parties;

(iv) Is not subject to a formal enforcement action or order by the Board, FDIC, or the OCC; and

(v) Has not experienced a change in control during the preceding 12-month period in which a full-scope, on-site examination would have been required but for this section.

(2) Discretionary standards. In determining whether an insured branch that meets the standards of paragraph (b)(1) of this section should not be eligible for an 18-month examination cycle pursuant to this paragraph (b), the FDIC may consider additional factors, including whether:

(i) Any of the individual components of the ROCA supervisory rating of an insured branch is rated 3 or worse;

(ii) The results of any off-site monitoring indicate a deterioration in the condition

of the insured branch;

(iii) The size, relative importance, and role of a particular insured branch when reviewed in the context of the foreign bank's entire U.S. operations otherwise necessitate an annual examination; and

(iv) The condition of the parent foreign bank gives rise to such a need.

(c) Authority to conduct more frequent examinations. Nothing in paragraphs (a) and (b) of this section limits the authority of the FDIC to examine any insured branch as frequently as it deems necessary.

By order of the Board of Directors.

Dated at Washington, DC, this 20th day of April, 1999.

FEDERAL DEPOSIT INSURANCE CORPORATION

(signed) Robert E. Feldman  
Robert E. Feldman,  
Executive Secretary.  
(SEAL)